89-1795

No. ___

Supreme Court, U.S.
FILED
MAY 15 1990
JOSEPH F. SPANIOL, JR.
CLERK

In The

Supreme Court of the United States

October Term 1989

BLUNT, ELLIS & LOEWI INCORPORATED,
JOHN FROMM and PETER PFEFFER,

Petitioners,

vs.

RONALD P. HLAVINKA and
JIMMIE G. DAVISON,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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May 15, 1990

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QUESTIONS PRESENTED

Whether the reparations provisions of the Commodity Exchange Act (7 U.S.C. § 18), permit a claimant to split his cause of action for monetary damages by proceeding to final judgment in the Commodity Futures Trading Commission (affirmed by the Seventh Circuit Court of Appeals), then immediately thereafter filing the same cause of action, asserting different legal theories for recovery, in state court?

Whether the "relitigation exception" to the Anti-Injunction Act (28 U.S.C. § 2283) requires a federal district court to enjoin such relitigation, at the petition of the parties prevailing in the first proceeding?

PARTIES IN THE PROCEEDING BELOW

Petitioners, Blunt, Ellis & Loewi, Incorporated, Peter Pfeffer and John Fromm, were petitioners in the proceeding below in the Seventh Circuit Court of Appeals. Ronald P. Hlavinka and Jimmie G. Davison, his attorney, were respondents in that proceeding. All of the above, except for Mr. Davison, were parties in the Commission reparations proceedings.

Blunt, Ellis & Loewi, Incorporated is a Delaware corporation and is wholly owned by Kemper Financial Services, Inc. ("KFSI") also a corporation. KFSI is wholly-owned by Kemper Corp., a Delaware corporation listed for trading on the New York Stock Exchange.

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vs.

RONALD P. HLAVINKA and JIMMIE G. DAVISON,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

Blunt, Ellis & Loewi, Incorporated ("Blunt"), John Fromm and Peter Pfeffer respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Seventh Circuit in this case.

OPINION BELOW

The opinion of the Court of Appeals (App. 2-4) is reported at 897 F.2d 240.

JURISDICTION

The judgment of the Court of Appeals (App. 1) was entered on February 16, 1990. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

STATUTES AND REGULATIONS INVOLVED

The relevant statutes and regulations, which are reproduced in relevant part in Appendix (App. 39-46), are Sec. 14(a), (b) and (e) and Sec. 22(a) and (c) of the Commodity Exchange Act (the "CEA"); codified at 7 U.S.C. § 18(a), (b) and (e) and 7 U.S.C. § 25(a) and (c). Sec. 2283 of the Judicial Code, 28 U.S.C. § 2283 is also involved. Commodity Futures Trading Commission (the "Commission") regulations are 17 CFR §§ 12.13(a), 12.15(a) and (b), and 12.24(a), (c) and (e).

STATEMENT OF THE CASE

When Congress established the Commission in 1974, it directed the agency to create an alternative adjudicative process permitting members of the investing public to elect to seek recovery of money damages by proceeding within the Commission. The purpose announced by Congress in adding the reparations provisions to the Commodity Exchange Act of 1974 (7 U.S.C. § 1, *et. seq.*), was to provide a speedy and efficient alternative to the other forums for litigation available to claimants.

Such claimants could elect to seek such recovery in a "reparations proceeding" for money damages allegedly caused by violations of the Act, or of any rule, regulation

or order issued pursuant to the Act. CEA § 14(a) (codified as 7 U.S.C. § 18(a)). Only the claimant may choose reparations as an alternative litigation forum; it is available, if chosen, as an alternative to litigation in the courts or arbitration. No person who claims to have been injured by such violations is required to present his complaint to reparations, but the Act affords him the option of proceeding there. The Commission's Director of the Office of Proceedings, after review, may decide to forward the complaint to the named respondents; thereupon the respondents must defend in the reparations forum if they are persons registered under the Act. 7 U.S.C. § 18(a); Comm. Reg. §§ 12.13(a) and 12.15(a); 17 CFR §§ 12.13(a), 12.15(a).

The only relief contemplated by the reparations section is the award by the Commission of money damages. The customer may apply to the Commission within two years after the *cause of action* accrues, " . . . for an order awarding actual damages proximately caused . . . " by violation of the Act or regulations. 7 U.S.C. § 18(a).

The trial level proceeding is before an administrative law judge ("ALJ"), who conducts the trial, views the witnesses, hears argument and then makes findings of fact, conclusions of law, and publishes the Initial Decision. The Act provides for an appeal of the ALJ decision to the entire Commission (17 CFR § 12.401); its determination may then be appealed to a federal court of appeals. CEA § 14(e); 7 U.S.C. § 18(e).

Ronald P. Hlavinka had been a commodity futures customer of Blunt, Ellis & Loewi, Incorporated ("Blunt") from 1980 onward, maintaining an account at one of Blunt's Milwaukee branch offices. The associated person

handling his account, beginning in 1982, was John Fromm. Peter Pfeffer was a vice president of Blunt at its headquarters in downtown Milwaukee and was in charge of its commodities futures activities at all fifty-plus branches.

From August 1982 onward, Hlavinka traded exclusively in silver futures contracts, making all of his own buy and sell decisions. Through February 14, 1983 profits had been realized on his silver futures trading, and Hlavinka had no open positions at the end of that day. He bought one May contract (5,000 oz.) on the Commodity Exchange of New York (the "COMEX") on Friday, February 18, then saw the market plunge the next trading day (February 22), but did not sell.

All commodity futures exchanges, the COMEX included, limit by rule the amount the trading price of a contract can fluctuate during any market session. On silver futures the COMEX price limit was $0.50 per oz., i.e. no trade would be recognized by the COMEX at a price greater than $0.50 above or less than $0.50 below the settlement price on the previous market day. The usual result of a "limit move" during a session is that trading virtually stops. If a "limit down" condition is reached, no buyer will normally be willing to purchase at the limit price, and the market is said to be "locked limit". Traders stand aside waiting for the next market day when new lower price limits will become effective.

The May contract "locked limit" down two days in succession, February 22 and 23. (Hlavinka was one of the only buyers on the 23rd, when he added a second contract to his holding). The COMEX rules provided for expanding the price limit to $0.75 per oz. if the market

closes at limit prices on two successive days. When the expanded price limit takes effect, it remains in effect for at least two market days. The firm handling Blunt's business on the floor of the COMEX (ACLI International, Inc.) incorrectly reported the limit to be $0.50 in its opening wire to the Blunt branch offices. No one became aware of that fact because the market traded freely throughout February 24, and up to near noon on the next day, never nearing a $0.50 move. Shortly before 1:00 p.m. on February 25 the prices broke downward through the $0.50 level, and a telephone call from Mrs. Hlavinka to Fromm caused Fromm to call the COMEX, from which he learned of the expanded price limit. He reported his discovery to Hlavinka, who then placed sell orders which could not be filled. The market was by then "locked" down the $0.75 limit, and it remained locked the entire following Monday.

On Tuesday, March 1, there was trading. Hlavinka kept one of his contracts and sold one. He sold the other contract the next day, realizing an aggregate loss on both contracts of $35,184.60. Five days later, he traded a 1,000 oz. contract, lost again and traded no more after March 7. His reparations complaint was filed with the Commission December 2, 1983.

Discovery[1] was had, after which a hearing was held before the Administrative Law Judge in a courtroom at the Milwaukee County Courthouse on July 14, 1986. Hlavinka, Fromm and Pfeffer each testified and was cross-examined. In October, the ALJ filed the Initial

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[1] Discovery is provided for in the Commission's Rules Relating to Reparations Proceedings, Part B. 17 CFR §§ 12.30-12.36.

Decision holding the COMEX rule, providing for expanded price limits after successive "limit" days, was immaterial to Hlavinka's claims, and that providing such expanded limits had no significant effect on market movements. (App. 19-20). The attempt by Hlavinka to establish a causal link between his losses and Fromm's unawareness of the expanded limit rule was found not persuasive. (App. 20). Finally, the ALJ found Hlavinka had not demonstrated he was determined to close his positions during the day and one-half in which he remained unaware of expanded price limits being in effect. (App. 22). The ALJ's decision dismissing the complaint was appealed to the full Commission, which found the ALJ to have been substantially correct; the Commission affirmed without opinion. (App. 24).

Hlavinka petitioned the Seventh Circuit Court of Appeals for review of the Commission's final order under CEA § 14(e). 7 U.S.C. § 18(e). In a six-page unanimous opinion, the Commission was affirmed. *Hlavinka v. Commodity Futures Trading Commission*, 867 F.2d 1029 (7th Cir., Feb. 6, 1989). (App. 26-38).

Relitigation in State Court

Sixteen days after the Court of Appeals' decision, Hlavinka (through his attorney, Jimmie G. Davison) filed a complaint in the Circuit Court of Milwaukee County (Wis.) based on the same core of operative facts the parties had litigated through the Commission and the Court of Appeals. (App. 13-15). Those facts, as alleged in the complaint, are that a contract was formed in August 1982 with Blunt "for services and advice in trading in the

Commodity Futures Exchange". (App. 14, ¶ 5). It is further alleged that Fromm " . . . on February 22nd [through] 25th, 1983 negligently failed to properly interpret market conditions and thus negligently failed to inform [Hlavinka] of the conditions". (App. 14, ¶ 9). Misrepresentations by defendants are alleged, i.e. that they were "experts in Commodities Futures and . . . were supposed to have the expertise to know the market conditions and keep [Hlavinka] informed at all times of market conditions." (App. 14, ¶ 7). Breach of contract, negligence and " . . . willfully fail[ing] to service the plaintiff even when they finally realized market conditions" are asserted as legal bases for an award of $35,000 in compensatory damages, plus $100,000 in punitive damages. (App. 14-15, ¶¶ 11, 12, 13).

Petitioners filed their petition for a permanent injunction and a stay of state court proceedings in the district court, basing federal jurisdiction on 28 U.S.C. § 1331 in that the relief requested was based on the relitigation exception to the Anti-Injunction Act, 28 U.S.C. § 2283, a law of the United States. This petition was filed before a responsive pleading was due in state court. The exception relied upon authorizes a court of the United States to grant an injunction to stay proceedings in State Court where such restraint is necessary for a court of the United States "to protect and effectuate its judgments". The district court denied the petition, concluding "Mr. Hlavinka had a right to pursue traditional state law claims – for things like negligence and breach of contract – against the petitioners. (App. 6-10, at 10).

The Seventh Circuit Court of Appeals held its final judgment in the first proceeding was not *res judicata* because the legal theories asserted in state court, i.e.

breach of contract and negligence, were not within the jurisdiction of the Commission. (App. 4). It omitted any mention of collateral estoppel. The Commission's own view that it had no jurisdiction over claims based upon violations of state law was given as a basis for the holding. (App. 4). No other authority is cited. The opinion does not indicate whether the cause of action was the same in both proceedings, or whether a change in legal theories created a new cause of action. It denied injunctive relief as to the breach of contract and negligence theories, but ordered the district court to enjoin relitigation of the fraud questions in state court. (App. 5).

REASONS FOR GRANTING THE WRIT

The impact of the two lower court opinions is to obliterate Congress's rationale for creating the reparations alternative. The declared intention of Congress in creating reparations was to provide customers of commodity brokerage firms with an extra-judicial forum which would be inexpensive and more expeditious than previously existing processes for dispute resolution. *See, S. Rep. No. 850, 95th Cong., 2d Sess. 11, 16 (1978).* The inevitable result of the court of appeals' holding is to invite aggrieved customers to split their claims, saving all pendant state law theories for "second effort" litigation in state court (or federal court, if diversity jurisdiction exists) in case the complainant is dissatisfied with the final judgment in reparations.

I. The Issues Presented Involve Important Questions Of Federal Law.

Neither opinion uses the term, but each necessarily endorses splitting a cause of action. Any aggrieved customer, whose complaint asserts that conduct by futures commission merchant ("FCM") employees violated the Act or Commission regulations, can go to judgment in reparations. If he prevails and is awarded damages which satisfy him, the case will be over. If he does not prevail, or if the award is less than the minimum acceptable, he has only to plead the same operative facts as supporting recovery under state law in court or to an arbitration tribunal. The second time he may assert that a contract was breached, a fiduciary duty had arisen and was breached, that actionable negligence was present, or any number of other legal theories for recovery; no legal theories will be precluded in the second proceeding except those based on alleged violation of the CEA or its related regulations.

Such second efforts may be constrained by statutes of limitations applicable to the state law claims, but nothing else. If the intended speedy determination in the Commission is realized, a disappointed claimant will launch his relitigation by filing suit asserting his non-CEA legal theories before any important such theory becomes time barred. If the reparations process has neared, but not reached, completion before such time constraint is encountered, the claimant will start anew in state *or federal* court, permitting the Commission's "parallel proceedings" regulation to nullify the entire preceding agency process. CFTC Reg. § 12.24(a) and § 12.24(c)(1); 17 CFR § 12.24(a) and (c)(1). A customer has an express private

right under the Act to bring his CEA-based claims in district court within two years after the date the cause of action accrued. CEA § 22(a)(1), and (c); 7 U.S.C. § 25(a)(1) and (c). Pendant jurisdiction may then be invoked to cover legal theories based on state law. If, on the other hand, there is a Commission judgment outside the two-year period, the claimant (under the Seventh Circuit's holding) can relitigate the cause of action, omitting only CEA-based claims. This will impose an intolerable and insupportable additional case load on already overburdened courts.

The reparations procedure, when invoked, must be the vehicle for resolving the entire dispute. This Court has already ruled Congress did not intend to require simultaneous litigation of the same issues before two different tribunals. *Commodity Futures Trading Commission v. Schor*, 478 U.S. 833 (1986). The Commission's "parallel proceeding" rule, *supra*, does not permit such simultaneous proceedings. The Commission's Director of the Office of Proceedings must refuse to institute reparations if the complainant has commenced arbitration or a civil court proceeding based on the same set of facts, or has asserted counterclaims which are so based. CFTC Reg. § 12.24(a) and § 12.24(c)(1). (App. 44-45). The initiation of such a proceeding after reparations has begun, but before the ALJ has decided the controversy and filed his initial decision, will cause a dismissal of reparations without prejudice. Reg. § 12.24(c)(2). (App. 45).

Petitioners respectfully urge the law cannot be that (1) counterclaims based on state law asserted by respondent must be determined in the same proceeding as the claims of the customer – and *Schor* holds they must be,

and (2) state law claims by the claimant, if asserted in any forum other than Commission reparations, will terminate the reparations proceeding, but (3) state law claims asserted by claimant *after* an unsatisfying final determination of a reparations proceeding will allow him to relitigate the same cause of action in state court. We urge this Court to require the claimant to assert all claims he intends to present, based on a single cause of action, in a single proceeding, whatever decisional forum he elects.

There are, at present, at least four statutes which permit proceeding for the recovery of money damages in a federal agency. *The Commodity Exchange Act*, 7 U.S.C. § 18; *The Packers and Stockyards Act*, 7 U.S.C. § 210; *The Shipping Act*, 46 U.S.C. § 821; *The Interstate Commerce Act*, 49 U.S.C. § 11,705. The holding below, if allowed to stand, is authority for a claimant splitting his cause of action under each such reparations provision. Commodity grievances alone will result in a significant increase in court actions by claimants whose prayer for money damages fails in the Commission. The extent to which customers have employed Commission reparations is published in the "Commodity Futures Trading Commission Annual Reports" for each year 1983 through 1989. These agency reports to Congress show

	1983	1984	1985	1986	1987	1988	1989
Reparations complaints filed	610	286	414	303	446	452	385
Disposed of by – Initial Decision	227	262	241	257	246	269	213

From 1983 onward, the Commission has disposed of 245 cases (on average) per year by initial decision.

The Seventh Circuit, in addition to opening the way for successive litigation on the same core of facts under four existing reparations schemes, has greatly reduced any judicial-efficiency incentive for Congress to create similar dispute resolution facilities in other regulated (or to-be regulated) areas of commerce.

No other circuit has addressed the issue of claim-splitting when the first proceeding is in reparations.

II. The Decision Below is Incorrect.

The Court of Appeals declined to distinguish or to comment upon holdings by this Court and by its own panels which reach contrary holdings involving similar principles. It would permit relitigation of the same cause of action in state court based solely on its conclusion that the Commission was without jurisdiction to adjudge alternate legal theories for recovery of money damages.

Petitioner respectfully asserts that the election of remedies doctrine, settled by this Court in *Terminal Warehouse Co. v. Pennsylvania R.R. Co.*, 297 U.S. 500 (1926), bars subsequent proceedings in court in situations where the claimant was not required to, but elected to pursue monetary damages in an agency upon which Congress had expressly conferred jurisdiction to award such damages. The Seventh Circuit has repeatedly held that *res judicata* prevents the splitting of a single cause of action and the use of several theories of recovery as the basis for sequential suits. *Shaver v. F.W. Woolworth Co.*, 840 F.2d 1361, 1365 (7th Cir., 1988). The opinion below declines to discuss either principle, which petitioners respectfully assert should be controlling.

A. The Decision Below Is In Conflict With This Court's Holdings.

Terminal Warehouse is the seminal "election of remedies" holding involving agency adjudication. It established that a plaintiff who seeks monetary relief in a regulatory body has elected the agency remedy, and cannot thereafter seek monetary relief before a court based on the same conduct. Election of remedies bars subsequent court proceedings where the regulatory proceeding was elected by the plaintiff, the acts of alleged wrongdoing are the same in both proceedings, monetary damages were the relief sought in the agency, Congress had conferred upon the agency jurisdiction to award monetary damages, and the agency proceeding was prosecuted to a final judgment. *Terminal Warehouse Co.*, 297 U.S. at p. 509. See dictum in *Carnation Co. v. Pacific Westbound Conference*, 383 U.S. 213, 224 (1966) (Permitting a plaintiff who had not sought monetary relief in an agency proceeding to sue for such relief in court did " . . . not suggest that petitioners might have sought recovery under both [the Shipping Act and the antitrust laws], but petitioner did have its choice.")

Other courts of appeals have addressed the claim that the agency was without jurisdiction to award relief on the theory asserted in the second proceeding. The voluntary election to begin in the agency, when recourse to Article III courts was available at the time such election was made, was held to preclude a second proceeding before a tribunal with jurisdiction to decide the theory advanced in the second case. The plaintiff is bound by the election even though dissatisfied with the remedy he

sought there. *Ellingson Timber Co. v. Great Northern Railway Co.*, 424 F.2d 497, 498 (9th Cir., 1970).

While under "election of remedies" it makes no difference whether the Commission was without jurisdiction to decide pendant claims, a recent decision of this Court suggesting the Commission could decide state law legal theories in reparations was ignored by the court of appeals. The *Schor* opinion clearly states there is no constitutional impediment to the reparations proceeding deciding common law claims having nothing to do with the Commodity Exchange Act. The Commission there decided a traditional contract issue based on state law which was presented to it as a counterclaim, and this Court approved.

The House of Representatives Report on the 1982 amendments to the CEA asserts "the reparations program seeks to pass upon the whole controversy surrounding each claim, . . . ". H.R. Rep. No. 565, 97th Cong., 2nd Sess., p. 55 (1982). If that is the intent of the legislature, the Commission may not frustrate that purpose by selectively adjudicating state law claims, deciding them only when they are presented as counterclaims. The *Schor* opinion strongly suggests Congress's delegation to the Commission of jurisdiction to award monetary relief necessarily implies conferring upon it pendant or ancillary jurisdiction. The opinion acknowledges the exercise of pendant jurisdiction may create constitutional difficulties greater than those presented by counterclaims, but

> " . . . we decline to endorse an absolute prohibition on such jurisdiction out of fear of where some hypothetical "slippery slope" may deposit us. Indeed, the CFTC's exercise of this type of

> jurisdiction is not without precedent. Thus, in *Reconstruction Finance Corp. v. Bankers Trust Co.*, 318 U.S. 163, 168-171 (1943), we saw no constitutional difficulty in the initial adjudication of a state law claim by a federal agency, subject to judicial review, when that claim was ancillary to a federal law dispute." *Schor*, 478 U.S. at p. 852.

Fromm's actions from February 22 through 25 were the core of the reparations suit, and whether they breached a contract or constituted negligence are questions clearly ancillary to the CEA-based claims.

Pendant jurisdiction, in the sense of judicial power, was created by the judicial branch without relevant action by Congress. *United Mine Workers of America v. Gibbs*, 383 U.S. 715, 725 (1966). The criteria relied upon for its recognition were (1) a federal claim of sufficient substance to confer subject matter jurisdiction on the court, (2) state and federal claims deriving from a common nucleus of operative fact, and (3) an ordinary expectancy that, without regard to the federal or state character of the various claims, such plaintiff's claims would be tried in one judicial proceeding. The same criteria strongly suggest that a federal agency, whose judgments are subject to judicial review, has jurisdiction to decide pendant state law claims as they arise in CEA reparations. A "sufficient substance" determination is mandatory, in that the Director of the Office of Proceedings is required to review the reparations complaint to determine whether the allegations assert that a specific provision of the Act or any rule, regulation or order thereunder has been violated by a covered person. 17 CFR 12.13(b) and 12.15(a). (App. 43). These state law claims inevitably arise from a common

nucleus of operative facts, being alternate legal theories put forward to support relief. One would surely expect these alternate legal theories based on the same facts to be tried in one adjudicatory proceeding.

The court of appeals refused to consider this Court's *Schor* analysis; that opinion is not cited at all. Neither does it consider the reason for, or application of, the principles on which pendant jurisdiction rests. It notes the Commission claims not to have such jurisdiction, and simply treats the Commission's stance as dispositive. There is no synthesis of the legislative interest (reparations should pass upon the *whole* controversy surrounding each claim), and the Commission's curiously self-contradicting position (i.e. it is competent and empowered to decide state law issues presented by counterclaimants but not by claimants).

Collateral estoppel, though argued by petitioners in both lower courts, was not referred to by either. The ALJ and the Seventh Circuit Court of Appeals, in the first proceeding, each held the failure to inform Hlavinka that expanded price limits were in effect was not a cause of his loss. *Parklane Hosiery Co., Inc. v. Shore*, 439 U.S. 327 (1979) establishes a losing party has no right to a jury trial where an issue essential to his success has been fully litigated by him, and decided against him in a prior proceeding. Four requirements must be present to establish collateral estoppel, and all appear to be present in this case.

> "(1) the issue to be precluded must be the same as that involved in the prior action; (2) the issue must have been actually litigated; (3) the determination made of the issue must have been

> essential to the final judgment; and (4) the party against whom estoppel is invoked must have been fully represented in the prior action." *Klingman v. Levinson*, 831 F.2d 1292, 1295 (7th Cir., 1987); see *International Association of Machinists & Aerospace Workers v. Nix*, 512 F.2d 125, 132 (5th Cir., 1975) (and cases cited therein).

If *Terminal Warehouse* continues to be the law (it has never been overruled), it makes no difference whether the Commission has jurisdiction over state law claims. Such could not be maintained in the second proceeding. If the analysis of *Schor* applies, including its recognition of the crippling effect a narrow reading of Commission jurisdiction would have on the purposes behind the reparations program (478 U.S. at p. 843), then *res judicata* bars the second state law suit. In either case, the decision below is contrary to holdings and analysis of this Court.

Most importantly, the opinion disregards the clear statements of policy this Court has made, and the objectives to be sought, in applying principles of *res judicata* and collateral estoppel. *Res judicata* is a part of our law because:

> "it is a rule of fundamental and substantial justice, of public policy and of private peace, which should be cordially regarded and enforced by the courts . . . " *Federated Department Stores, Inc. v. Moitie*, 452 U.S. 394, 401 (1981), quoting *Hart Steel Co. v. Railroad Supply Co.*, 244 U.S. 294, 299 (1917).

Fundamental and substantial considerations of justice require:

> " . . . that there be an end of litigation; that those who have contested an issue shall be bound by the result of the contest, and that matters once

> tried shall be considered forever settled as between the parties." *Baldwin v. Iowa State Traveling Men's Association*, 283 U.S. 522, 525 (1931)."

Res judicata and collateral estoppel are intended to promote justice by ensuring the finality of decision. *Brown v. Felsen*, 442 U.S. 127, 131 (1979).

None of the policies or recent holdings of this Court, no interest of the federal system, and nothing which would enhance the effectiveness of state courts, arbitration forums, or the adjudicatory function of administrative agencies is advanced by permitting this decision of the court of appeals to stand as a precedent.

B. The Decision Below Conflicts In Principle With The Seventh Circuit's Own Decisions And The Decisions Of Other Circuits

The court of appeals held that a cause of action may be split if the first litigation forum chosen by the claimant has jurisdiction to decide only some (but not all) of the legal theories capable of assertion. The Seventh Circuit Court of Appeals has repeatedly held that the doctrine of *res judicata* bars not only those issues which were actually decided in the prior action but also any issues which could have been raised. *Shaver v. F.W. Woolworth Co.*, 840 F.2d 1361, 1364 (7th Cir. 1988); *Lee v. City of Peoria*, 685 F.2d 196, 198 (7th Cir., 1982) and *Whitely v. Seibel*, 676 F.2d 245, 248 (7th Cir., 1982).

The "cause of action" has been the pivot of *res judicata* analysis. If the "cause of action" in the second suit is the same as that in the first, *res judicata* bars the second suit. Federal law defines a single cause of action as "a

core of operative facts which give rise to a remedy". *In the Matter of Energy Cooperative, Inc.*, 814 F.2d 1225, 1230-31 (7th Cir., 1987), quoting *Car Carriers, Inc. v. Ford Motor Co.*, 789 F.2d 589, 593 (7th Cir., 1986), based on *Restatement (Second) of Judgments*, § 24 (ALI, 1982) ("Once a transaction has caused injury, all claims arising from that transaction must be brought in one suit or lost"). The state court complaint shows the core of operative facts is identical in both suits; neither counsel for plaintiff nor either lower court has ever expressed disagreement with that statement.

The only change from Hlavinka's 1983 filing to that made in 1989 is in legal theories for recovery, but the Seventh Circuit has repeatedly held that such a change does not create a new cause of action. *Car Carriers, Inc.*, supra; *Alexander v. Chicago Park District*, 773 F.2d 850, 854 (7th Cir., 1985); *Shaver*, 840 F.2d at p. 1365. Other circuits have also held that when two successive suits seek recovery for the same injury, judgment on the merits in the first operates as a bar to the later suit, even though a different legal theory of recovery is advanced in the second suit. *Cemer v. Marathon Oil Co.*, 583 F.2d 830, 832 (6th Cir. 1978); *Pasterczyk v. Fair*, 819 F.2d 12, 15 (1st Cir., 1987); *McClain v. Apodaca*, 793 F.2d 1031, 1034 (9th Cir., 1986).

Res judicata is applicable where the judgment in the first suit was by an administrative agency. This Court has so held, requiring that the agency must have (1) acted in a judicial capacity, (2) resolved disputed issues of fact properly before it, and (3) afforded the parties an adequate opportunity to litigate the cause of action. *U.S. v. Utah Construction & Mining Co.*, 384 U.S. 394, 421-2 (1966).

When those conditions have been met – and they were met in the Commission proceeding – the agency's determinations are accorded the same finality as a court judgment. *University of Tennessee v. Elliott*, 478 U.S. 788, 798 (1986). The Seventh Circuit has so held in *Button v. Hardin*, 814 F.2d 382, 384 (7th Cir., 1987), as has the Fifth Circuit. *International Association of Machinists & Aerospace Workers v. Nix*, 512 F.2d 125 (5th Cir., 1975) (ordering an injunction against a state court proceeding for breach of contract, filed after plaintiff had lost an unfair labor practice claim in the NLRB).

After a matter has been fully litigated to final judgment in the federal system, it is essential that the relitigation exception to 28 U.S.C. § 2283 be employed to prevent imposing upon the prevailing party the burden of having to prevail a second time in litigating the same cause of action. The relitigation exception was designed to permit a federal court to prevent state litigation of a cause of action or an issue that previously was presented to and decided by the federal court. As this Court recently wrote, the relitigation exception "is founded in the well-recognized concepts of *res judicata* and collateral estoppel." *Chick Kam Choo v. Exxon Corp.*, 486 U.S. 140, 147 (1988). For the federal judiciary to fail to issue such injunctions would result in a federal judgment coming to nothing that is final. See, *Toucey v. New York Life Ins. Co.*, 314 U.S. 118, 144 (1941), Mr. Justice Reed's dissent. (The Revision Notes declare that Sec. 2283, as revised in 1948, restores the basic law as generally understood and interpreted in Mr. Justice Reed's dissent; see U.S.C.A. 28 U.S.C. § 2283, p. 3 (1978)).

That the exceptions to the Anti-Injunction Act are narrow, and not to be enlarged by loose statutory construction, does not undermine the necessity for federally mandated prevention of relitigation in the reparations context. The federal judiciary's interest in assuring the integrity of federal judgments is both essential and compelling. The role of such injunctions is vital to preserve federal court authority, and to avoid needless litigation which threatens to choke all dispute resolution tribunals. *Amalgamated Sugar Co. v. NL Industries, Inc.*, 825 F.2d 634, 639 (2d Cir. 1987). When the relitigation exception is invoked prior to a state court decision on *res judicata* or collateral estoppel, such injunctions should issue. The alternative is to force the winner in federal court to go through the entire state appeals procedure hoping the state court perceives that the issues before it formed the basis of a prior federal judgment. *Nix* at p. 132. A winner in federal court should not be deprived of his victory, tnen exposed to the possibility of a later contrary state judgment which this Court may or may not review. *Woods Exploration and Producing Co. v. Aluminum Co. of America*, 438 F.2d 1286, 1312 (5th Cir., 1971); see also, *Meridian Investing & Development Corp. v. Suncoast Highland Corp.*, 628 F.2d 370, 373 (5th Cir., 1980).

Collateral estoppel principles apply to the essential issues of causation respecting Hlavinka's breach of contract theory and his negligence theory. The judgment by the ALJ was that Hlavinka's attempt to establish a causal link between unawareness of the expanded price limits and his losses was unpersuasive. (App. 20). The Seventh Circuit held that Hlavinka's losses were not caused by the broker's failure to tell him of the expanded limit rule.

(App. 32, 37). A breach of contract which is not the proximate cause of a loss cannot support recovery, nor can negligence not causing injury. The issue of causation was clearly decided in the first suit.

The Fifth Circuit upheld an injunction to prevent relitigation in state court of a cause of action previously decided by a federal agency (the National Labor Relations Board), and affirmed by the court of appeals. Nix's unfair labor practice charges, rejected in the first proceeding, were cast as breach of contract in state court. Though the NLRB had no jurisdiction to adjudge state law breach of contract claims, the principles of collateral estoppel barred the claims, and an injunction issued. *International Association of Machinists & Aerospace Workers v. Nix*, supra, 512 F.2d at p. 132.

There is Seventh Circuit law that a federal court *must* enjoin subsequent state court proceedings in these circumstances. *Samuel C. Ennis & Co., Inc. v. Woodmar Realty Co.*, 542 F.2d 45, 49 (7th Cir., 1976) (the court of appeals reversed a district court refusal to enjoin state proceedings because the relitigation exception required such restraint). The same court affirmed such an injunction when the unsuccessful federal litigant claimed breach of contract in state court. *Harper Plastics v. Amoco Chemicals Corp.*, 657 F.2d 939, 947 (7th Cir., 1981).

C. This Court Should Settle The Question Of Permitting Claim-Splitting By A Claimant Who Elected To Proceed In A Forum Exercising Limited Jurisdiction.

The "election of remedies" doctrine, first applied in *Terminal Warehouse*, held that a claimant's election to seek

monetary relief in an agency empowered by Congress to grant such remedy, but of lesser breadth than remedies attainable in Article III courts, precluded a second proceeding seeking broader remedies based on the same acts of alleged wrongdoing. Two decades later, the denial of a money claim by an agency was said to bar the door to redress in the courts. *Elgin Joliet & Eastern Ry. Co. v. Burley*, 325 U.S. 711, 761 (1945). As recently as 1988, a district court wrote that the *res judicata* effect of an agency decision adjudicatory in character was "essentially black letter law." *Washington v. Sec. of Health Education and Human Services*, 693 F.Supp. 569, 573 (N.D. Ohio, 1988).

The term, "election of remedies", has come to mean two different things. It comes up most often within the framework of a single judicial proceeding, e.g. where the relief sought is both rescission and money damages. The *Terminal Warehouse* "election of remedies" contemplates a choice of forums (administrative or judicial), each capable of awarding money damages but where the administrative agency is, or may be, constrained by the legislative grant under which the subject jurisdiction is exercised.

One member of the court of appeals panel (Hon. Hubert Will, sitting by designation) commented during the oral argument that he found it difficult to believe there was no reported case addressing these issues arising from Commission reparations. For reasons not explained, the court of appeals made no mention of apparently controlling precedents which arose under the Interstate Commerce Act or the Shipping Act. We respectfully submit there is no material difference between application of the *Terminal Warehouse* rule to reparations under the CEA than to agency proceedings for monetary

reparations under the earlier legislation applicable to other areas of commerce.

It is in the obvious interest of this Court, and all courts, that those who have contested an issue shall be bound by the result of the contest, and that matters once tried shall be forever settled between the parties. By declining to discuss apparently controlling case law, the court of appeals necessarily implies its view that changed conditions have changed the agency "election of remedies" doctrine. This Court should grant certiorari to settle whatever question remains about the application of these principles to agency reparations proceedings in conditions existing nearly three quarters of a century after the *Terminal Warehouse* holding.

D. The Decision Below Runs Directly Contrary To The Express Intention Of Congress.

The creation of the reparations option, permitting (but not requiring) an aggrieved customer to seek money damages in the Commission instead of in the courts or arbitration, was intended by Congress to provide such persons with a voluntary alternative which would be less expensive and speedier than court or arbitral litigation. *S. Rep. No. 850, 95th Cong., 2d Sess. 11, 16 (1978).*

Furthering this clear intention, Congress amended the reparations provisions in 1982, partly to streamline the process; in that context, the House Report declares " . . . the reparations program seeks to pass upon the whole controversy surrounding each claim, including counterclaims arising out of the same set of facts . . . ". *H. R. Rep. No. 565, 97th Cong., 2d Sess. 55 (1982).*

The expressed objective of Congress is fully consistent with the objective of the courts: to dispose of the entire controversy whether the initiator submits that controversy to a court, to arbitration or to reparations. The court of appeals' decision runs directly against the intent of Congress so expressed. This Court should review that decision and, if indicated, correct it.

CONCLUSION

Petitioner respectfully urges this Court to settle questions left unaddressed by the court of appeals, but of great importance to the administration of law in this period of bloated and increasing dockets of all dispute-resolution tribunals. The agency "election of remedies" doctrine needs to be applied with no less vigor than was demanded in 1926. *Res judicata* and collateral estoppel must limit the trial of a claim or dispositive issue to one fully-reviewed proceeding. The instrument for insuring the vitality of those principles applied to litigation in federal forums, whether court or agency, is the injunction, employed to prevent the kind of relitigation expressly and necessarily exempted from 28 U.S.C. § 2283. Certiorari should be granted to resolve this important question of federal law for all federal circuits.

Respectfully submitted,

BLUNT, ELLIS & LOEWI, INCORPORATED, JOHN FROMM, AND PETER PFEFFER, Petitioners

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DATE: May 15, 1990

APPENDIX

App.

Judgment Order, February 16, 1990 1

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JUDGMENT – ORAL ARGUMENT
UNITED STATES COURT OF APPEALS

For the Seventh Circuit
Chicago, Illinois 60604

February 16, 1990

Before
Hon. William J. Bauer, Chief Judge
Hon. Walter J. Cummings, Circuit Judge
Hon. Hubert L. Will, Sr. District Judge*

BLUNT, ELLIS & LOEWI, INCORPORATED, JOHN FROMM and PETER PFEFFER,	)	Appeal from the United States District Court for the Eastern District of Wisconsin.
Plaintiffs-Appellants,	)	
No. 89-2265 v.	)	
RONALD P. HLAVINKA and JIMMIE G. DAVISON,	)	No. 89 C 432
Defendants-Appellees.	)	Terrence T. Evans, Judge

This cause was heard on the record from the United States District Court for the Eastern District of Wisconsin, ___ Division, and was argued by counsel.

On consideration whereof, IT IS ORDERED AND ADJUDGED by this Court that the judgment of the said District Court in this cause appealed from be, and the same is hereby, AFFIRMED IN PART, with costs, and REMANDED IN PART, in accordance with the opinion of this Court filed this date.

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* The Honorable Hubert L. Will, Senior District Judge for the Northern District of Illinois, is sitting by designation.

Reported at 897 F.2d 240

UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

No. 89-2265

BLUNT, ELLIS & LOEWI, INC.
JOHN FROMM and PETER PFEFFER,

Petitioners-Appellants,

v.

RONALD P. HLAVINKA and
JIMMIE G. DAVISON,

Respondents-Appellees.

ARGUED JANUARY 1990 – DECIDED
FEBRUARY 16, 1990

Before BAUER, Chief Judge, CUMMINGS, Circuit Judge, and WILL, Senior District Judge. The Honorable Hubert L. Will, Senior District Judge for the Northern District of Illinois, is sitting by designation.

CUMMINGS, Circuit Judge. In December 1983, respondent Ronald Hlavinka initiated a reparations action before the Commodity Futures Trading Commission under Section 14 of the Commodity Exchange Act ("CEA") (codified at 7 U.S.C. § 18) against petitioners Blunt, Ellis & Loewi, Inc. and its employees, John Fromm and Peter Pfeffer, complaining that he had lost $27,500[1] in trading silver futures contracts. Hlavinka claimed that this corporate registered futures commission merchant and its employees had given him false information in violation of the anti-fraud provision of the CEA (7 U.S.C. § 6b). An

administrative law judge ("ALJ") concluded that Hlavinka was not damaged by the violation of this statutory provision or by violation of a Commission regulation. CCH Comm. Fut. L.R. ¶23,324 (1986). The Commission summarily affirmed the ALJ's dismissal of the complaint[2] and we affirmed the Commission's order. *Hlavinka v. Commodity Futures Trading Commission*, 867 F.2d 1029 (1989). About a fortnight thereafter, Hlavinka filed a complaint in the Circuit Court of Milwaukee County, Wisconsin, against the same firm and licensed stockbrokers. The complaint alleged that in August 1982 Hlavinka entered into a contract with the defendant firm for services and advice in trading on the Commodity Futures Exchange. The complaint was based upon breach of contract and negligence and sought $35,000 compensatory damages and $100,000 punitive damages.

Three months thereafter, the defendants in the state court action filed a federal lawsuit against Hlavinka and Jimmie Davison, his attorney, seeking an injunction and stay with respect to processing the state court complaint. The federal plaintiffs rested their request on a claim of res judicata on the ground that the same core of operative facts was involved in the state court suit as in the complaint processed by the Commission. The district judge denied any relief on the ground that breach of contract and negligence claims were not within the jurisdiction of the Commission. Consequently, he held that the CEA does not preempt all state law claims. We affirm.

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[1] The damages claimed increased to approximately $35,500.

[2] Reported in CCH Comm. Fut. L.R. 23,906 (1987).

It is noteworthy that the Commission has filed an amicus brief asserting that it does not have jurisdiction over claims which do not violate any provision of the CEA or Commission rule, regulation or order thereunder. Therefore the Commission itself maintains it had no jurisdiction over any claims of Hlavinka based upon violations of state law such as the breach of contract and negligence claims involved in his complaint now pending in the Milwaukee County Circuit Court.

This case is governed by the Anti-Injunction Act (28 U.S.C. § 2283), which provides as follows:

> **§ 2283. Stay of State court proceedings**
>
> A court of the United States may not grant an injunction to stay proceedings in a State court except as expressly authorized by Act of Congress, or where necessary in aid of its jurisdiction, or to protect or effectuate its judgments.

Petitioners have not shown that the Commission had any jurisdiction over negligence or breach of contract tort claims such as contained in the Wisconsin suit brought by Hlavinka. Consequently, its dismissal of Hlavinka's administrative complaint is not res judicata as to the breach of contract and negligence claims he has brought in state court. Accordingly, the broad injunction sought by petitioners is not permissible under 28 U.S.C. § 2283.

While we agree with the district court that Hlavinka is entitled to pursue his breach of contract and negligence claims in state court, Hlavinka may not rely upon fraud in that forum because that matter was fully litigated before the Commission and before this Court. The Supreme Court has recognized that the exceptions to the

Anti-Injunction Act are narrow and not to be enlarged by loose statutory construction. *Chick Kam Choo v. Exxon*, 486 U.S. 140, 147. However, to protect petitioners from again defending the question decided by the Commission, on remand they are entitled to an injunction restraining Hlavinka and his counsel from relitigating the question of fraud. This will effectuate our judgment in the 1988 appeal and therefore is within the express exception to the Anti-Injunction Act that permits an injunction to effectuate a federal judgment.

Because Hlavinka is not barred from pursuing his state court remedy, the petitioners' request for sanctions plus costs and attorney's fees is of course meritless.

Affirmed in part; remanded in part.

Reported at 711 F.Supp. 950

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF WISCONSIN

BLUNT, ELLIS & LOEWI, INC.
JOHN FROMM and
PETER PFEFFER,

Petitioners

-vs-

Civil Action
No. 89 C 432

RONALD P. HLAVINKA and
JIMMIE G. DAVISON, et al.,

Respondents.

ORDER

Blunt, Ellis & Loewi, Inc., John Fromm, and Peter Pfeffer have filed this lawsuit seeking an injunction against Ronald P. Hlavinka and Jimmie G. Davison. Blunt Ellis is a registered futures commission merchant in Milwaukee. Fromm and Pfeffer are employees of Blunt Ellis. Mr. Hlavinka was a customer of Blunt Ellis who lost his shirt – to the tune of some $35,000 – when the silver futures market fell precipitously during a one-week period starting near the end of February, 1983. Mr. Davison has acted as Mr. Hlavinka's lawyer during prior legal proceedings which sought compensation for the losses Hlavinka sustained.

Blunt, Ellis, Fromm, and Pfeffer seek to enjoin Hlavinka and Davison from pursuing any claim set forth in a recently filed complaint in a Milwaukee County Circuit Court case. The petitioners also seek an order

directed to the Circuit Court of Milwaukee County that will, in effect, stay any proceedings in that court that relate to the complaint. The state court case, number 89-CV-02529, is assigned to Milwaukee County Circuit Court Judge Victor Manian. A hearing was held before me on the request for injunctive relief on May 3, 1989.

The petitioners rest their request for injunctive relief and a stay of the state court proceedings on a claim of *res judicata*. In a nutshell, the dispute here concerns losses sustained by Mr. Hlavinka while dealing in silver futures transactions between February 22 and the first few days of March of 1983. After the losses were incurred, Mr. Hlavinka filed a claim against the petitioners with the Commodity Futures Trading Commission. Mr. Hlavinka's claims were heard by an administrative law judge who ultimately found in favor of the petitioners. The Commodity Futures Trading Commission affirmed the decision of the administrative law judge following an administrative appeal, and the United States Court of Appeals for the Seventh Circuit ultimately affirmed that finding when Mr. Hlavinka sought review in that forum. *Hlavinka v. CFTC*, 867 F.2d 1029 (7th Cir. Feb. 6, 1989).

Arguing that Hlavinka's state court complaint – where he has sued the petitioners for breach of contract – arises from the same core of operative facts as did the complaint he filed with the Commodity Futures Trading Commission, the petitioners seek an order prohibiting the prosecution of the complaint in state court.

The Commodity Exchange Act (CEA), 7 U.S.C. § 1 *et seq.*, broadly prohibits fraudulent and manipulative conduct in connection with commodity futures transactions.

In 1974, Congress overhauled the act in order to institute a more "comprehensive regulatory structure to oversee the volatile and esoteric futures trading complex." H.R. Rep. No. 93-975 at 1 (1974). See Pub. L. No. 93-463, 88 Stat. 1389. Congress also determined that the broad regulatory powers of the CEA were most appropriately vested in an agency which would be relatively immune from the "political winds that sweep Washington." H.R. Rep. No. 93-975 at 44, 70. It therefore created an independent agency, the Commodity Futures Trading Commission (CFTC), and entrusted to it sweeping authority to implement the CEA.

Among the duties assigned to the CFTC was the administration of a reparations procedure through which customers – particularly disgruntled ones like Mr. Hlavinka – of registered commodity brokers could seek redress for the brokers' violations of the act or CFTC regulations. The CEA provides that any person injured by such violations may apply to the commission for an order directing the offender to pay reparations to the complainant. An award of damages against the broker is enforceable in federal district court. Congress intended this administrative procedure to be an "inexpensive and expeditious" alternative to existing forums available to aggrieved customers, namely, the courts and arbitration. S. Rep. No. 95-850 at 11 (1978), *reprinted in* 1978 U.S. Code Cong. & Admin. News 2087, 2099. *See also* 41 Fed. Reg. 3994 (1976) (accompanying CFTC regulations promulgated pursuant to § 14).

The issue presented is whether a customer – like Hlavinka here – can choose a forum – like the CFTC's reparations procedures – lose there, and then press a state

law cause of action in state court growing essentially out of the same set of facts. Although it seems like a terribly inefficient way to run a railroad, I reluctantly conclude that he can. That is not to say, however, that the judge in state court might not find some sort of estoppel here or might not conclude that the CFTC's findings entitle the petitioner to summary judgment on the state law claims. These are matters best left to Judge Manian.

I reach my conclusion here, as I said, reluctantly. I say reluctantly because in conformance with the congressional goal of promoting efficient dispute resolution, the CFTC promulgated a regulation in 1976 which allows it to adjudicate counterclaims arising out of the transaction or occurrence or series of transactions or occurrences set forth in the complaint. Unfortunately, the CFTC does not request that *all* claims and *all* theories of recovery that a customer has against a broker – particularly those based on state law – be included in a reparations complaint. And it is doubtful whether all could be. The CFTC seems more concerned with violations of its rules, fraudulent conduct on the behalf of brokers, and the like. Mere negligence, or simple breach of contract claims, may not even be covered by the CEA. For as the court of appeals noted, Hlavinka's reparations case bit the dust partly because "for commodities fraud, negligence is not enough." 867 F.2d 1029 at 1033.

Counterclaims by brokers – permitted by the 1976 regulation – are permissive. They leave a broker free, if he wishes, to seek relief against a reparations complainant in other forums. *Commodity Futures Trading Comm'n v. Schor*, ___U.S.___, 106 S. Ct. 3245 (1986). The fact that the procedure is permissive, I think, saves it from violating

Northern Pipeline Construction Co. v. Marathon Pipe Line Co., 458 U.S. 50, 102 S. Ct. 2858 (1982), in which the United States Supreme Court held that Congress may not vest in a non-Article III court the power to adjudicate, render final judgment, and issue binding orders in a traditional contract action arising under the state law without the consent of the litigants.

In this case, Mr. Hlavinka had a right to pursue traditional state law claims – for things like negligence and breach of contract – against the petitioners. Among other things, he had a potential right to have a jury hear his grievances. Absent some clearer authority that Congress wanted (or that the Constitution would permit) the CEA to preempt all state law claims and transfer them to non-Article III administrative judges in CFTC hearings, I conclude that the petitioners' request for an injunction and stay must be DENIED.

The issue here is close. Merit abounds on both sides. Accordingly, both sides' motions for Rule 11 sanctions based on frivolity are also DENIED.

SO ORDERED at Milwaukee, Wisconsin this 18th day of May, 1989.

BY THE COURT:

TERENCE T. EVANS
UNITED STATES DISTRICT JUDGE

Not Reported

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF WISCONSIN

BLUNT, ELLIS & LOEWI, INC.
JOHN FROMM and PETER
PFEFFER,

Petitioners

-vs-

Civil Action
No. 89-C-432

RONALD P. HLAVINKA and
JIMMIE G. DAVISON, et al.,

Respondents.

ORDER

The petitioners have filed a motion asking me to reconsider my order of May 18, 1989. The order denied a request to issue an injunction and stay proceedings in a state court case filed against the petitioners by Mr. Hlavinka. The petitioners assert that my decision "runs directly contrary to both the holding and the reasoning of *Harper Plastics, Inc. v. Amoco Chemical Corp.*, 657 F.2d 939 (7th Cir. 1981). The motion is DENIED.

In my view, the petitioners misread the *Harper Plastics* case. In that case, the court of appeals considered whether *res judicata* bars a litigant from bringing a contract claim in state court following a dismissal on the merits of his federal antitrust claim in a federal district court. The difference between *Harper Plastics* and this case is both basic and simple. In *Harper Plastics*, the plaintiff could have joined his state law claims in his

federal suit. Had he done so, his claims would have been resolved by an Article III judge. In this case, the administrative judge had no jurisdiction to entertain state law claims. They could not have been joined even through, under the peculiar circumstances of reparation proceedings, a counterclaim by a registered broker could have been entertained. Accordingly, I stand by the decision I entered on May 18, 1989. The motion for reconsideration is DENIED.

SO ORDERED at Milwaukee, Wisconsin this 2nd day of June, 1989.

BY THE COURT:

TERENCE T. EVANS
UNITED STATES DISTRICT JUDGE

STATE OF WISCONSIN CIRCUIT COURT
MILWAUKEE COUNTY

RONALD P. HLAVINKA,

Plaintiff,

v.

BLUNT, ELLIS & LOEWI, INC. JOHN FROMM AND PETER PFEFFER,

Defendants.

FILED:
February 22, 1989
COMPLAINT
Case No. 89
CV 02529

NOW COMES the above-named plaintiff, Ronald P. Hlavinka, by his attorney, Jimmie G. Davison, and as for a claim of relief against the above-named defendants, alleges and shows to the Court as follows:

1. That Ronald P. Hlavinka is an adult resident of the City of New Berlin, County of Milwaukee, Wisconsin.

2. That the defendant, Blunt, Ellis and Loewi, Inc., on information and belief is a domestic corporation, with principal offices in Milwaukee, Wisconsin.

3. That the defendant, John Fromm, on information and belief is a licensed stock broker in the employment of the defendant, Blunt, Ellis and Loewi, Inc.

4. That the defendant, Peter Pfeffer, is on information and belief a licensed stock broker in the employment of the defendant Blunt, Ellis & Loewi, Inc., as a stock broker supervisor.

5. That the plaintiff entered into a contract, at the urging and invitation of the defendants, in August, 1982, with the defendant Blunt, Ellis and Loewi, Inc. for services and advice in trading in the Commodity Futures Exchange.

6. That the defendant Blunt, Ellis and Loewi, Inc. assigned the defendant John Fromm to be the broker servicing the plaintiff.

7. That the defendant, Blunt, Ellis and Loewi, Inc. represented themselves to the plaintiff as experts in Commodities Futures and pursuant to Contract the defendants and/or their agents were supposed to have the expertise to know the market conditions and keep the plaintiff informed at all times of market conditions.

8. That the defendant John Fromm set himself out as an expert in interpreting market conditions and the plaintiff relied on this apparent expertise.

9. That the defendant John Fromm on February 22nd, 23rd, 24th and 25th, 1983, negligently failed to properly interpret market conditions and thus negligently failed to inform the plaintiff of the conditions.

10. That the defendant, Peter Pfeffer, negligently failed to properly supervise defendant John Fromm on the dates mentioned above.

11. That the defendants willfully failed to service the plaintiff even when they finally realized market conditions.

12. That because of the above mentioned negligence the defendant Blunt, Ellis and Loewi, Inc. breached the contract it entered into with the plaintiff.

13. That because of the breach of contract and negligence of the defendants, the plaintiff suffered a financial loss in the amount of $35,000.

14. That because of the breach of contract and negligence of all of the defendants, the plaintiff suffered great mental stress and anguish.

WHEREFORE, the plaintiff, Ronald P. Hlavinka, prays for judgment against the defendants, jointly and severally, as follows:

a. Compensatory damages in the amount of Thirty-five Thousand Dollars ($35,000).

b. One Hundred Thousand Dollars ($100,000) for punitive damages for defendants' wilful failure to service the plaintiff at a time when they finally realized the plaintiff was in danger and could be helped.

c. Costs and disbursements of this action along with attorney fees and any other relief this Court deems just and equitable.

Dated at Milwaukee, Wisconsin this 21st day of February, 1989.

Respectfully submitted,

LAW OFFICES OF
JIMMIE G. DAVISON

Jimmie G. Davison
Attorney for Plaintiff

Address

633 West Wisconsin Avenue
Suite 607
Milwaukee, Wisconsin 53203

Reported at CCH Commodity Futures L.R. ¶23,324 (1986)

UNITED STATES OF AMERICA
Before the
COMMODITY FUTURES TRADING COMMISSION

RONALD P. HLAVINKA,
Complainant

v.

BLUNT, ELLIS & LOEWI, et al.,
Respondents

CFTC Docket
No. 84-R117

Appearances:

Ronald P. Hlavinka, pro se.

Thomas P. Ward, Esq., for respondents.

INITIAL DECISION

Shipe, Administrative Law Judge:

This proceeding was instituted on February 4, 1984, by the forwarding of the complaint and answers to the Proceedings Clerk for assignment. The proceeding is brought pursuant to Section 14 of the Commodity Exchange Act as amended (7 U.S.C. §18).

The complainant makes various allegations of mishandling of his account by respondents, which if proved, would constitute violations of the Act. Respondents deny that any of their actions were violative of the Act, or were the cause of complainant's admitted losses.

An oral hearing was conducted on the matter in Milwaukee, Wisconsin, on July 14, 1986.

Based upon the entire record, including the demeanor of the witnesses at the oral hearing, the following

Findings of Fact, Discussion of Facts and Law, and Order, are entered.

FINDINGS OF FACTS

1. The complainant is a supervisor at Patrick Cudahy. Tr. 9. On a form signed on January 3, 1980, in connection with opening a commodity account with Blunt, Ellis & Loewi, Incorporated (BEL), complainant listed his liquid net worth (cash) as $100,000 and other equity as $250,000, with risk capital of $5,000 available for trading commodities. He gave his occupation, "Real Estate Invest." Ex. R101.

2. BEL is a registered futures commission merchant with offices in Milwaukee, Wisconsin. Respondent John Fromm (Fromm) was at the time relevant here an associated person with BEL. Respondent Peter J. Pfeffer was head of BEL's commodity division. Tr. 45, 81.

3. Complainant opened a commodity account with BEL in January 1980. After losing money, he ceased trading for about one year, but resumed trading August 1982. He had taken and made delivery of silver bullion during the unprofitable trading period. Tr. 17-18; Ex. 103-180.

4. Prior to January 1983, complainant traded 1000-ounce silver contracts on the Chicago Board of Trade. Beginning in January 1983, against the advice of Fromm, his account executive at BEL, he began trading 5,000-ounce silver contracts on the Commodity Exchange, Inc. (COMEX). Following a series of such trades, which were profitable, complainant closed a contract on February 14,

1983, leaving the account without positions. Tr. 21; Account Statements.

5. On February 18, 1983, he bought one 5,000-ounce contract at $14.84 per ounce. Tr. 21. On February 23, 1983, complainant's wife, with his concurrence bought one additional such contract at $13.81. Tr. 7-8.

6. On February 23, 1983, the involved contracts closed "down the limit" at $13.80. On February 24, 1983, trading took place within the daily limits. Complainant placed a limit order to sell one of his contracts, but it was not filled. Ex. R104; Ex. R111.

7. February 25, 1983, was a Friday. On that day trading took place. At about 12:45 p.m., local time, complainant's wife called Fromm for a price quotation, and learned that the market was down 52 cents. Fromm was not able to explain how the price could have dropped 52 cents below the closing price of the previous day, since both he and Mrs. Hlavinka believed that the daily price limit was 50 cents. Tr. 10, 99. In fact, the limit had been expanded, pursuant to an exchange rule, because of limit movements on prior days. Ex. R108. Before closing on February 25, the market again was locked down the limit. Ex. R107-125. Complainant placed a market order near the close, but it was not filled. Ex. R113. On the following day, March 1, complainant first placed an order to sell one contract, which was executed. Ex. R. 114. After the market had again locked down the limit, complainant placed an order to sell the remaining contract, but it was not filled. Ex. R115. On March 2, after first placing a limit order that failed to be executed, complainant placed a market order which was filled. Ex. R116.

8. - On the two 5000-contracts, he lost a total of $35,184.60. Acct. Statements.

9. On March 7, 1985, complainant day-traded a 1000-ounce silver contract at a loss of $281.06. Acct. Statements.

DISCUSSION OF FACTS AND LAW

The complainant predicates virtually his entire case on the circumstance that Fromm was not aware on February 25, 1983, that under COMEX rules the price limits on the involved contracts had, because of previous limit moves in the market, expanded to 75 cents. He argues that if he had been informed of the described rule he would not have placed the contract on February 23, 1983, and would have closed both of his contracts on February 24, 1983.

In legal terms the issue boils down to whether this COMEX rule was a material fact which respondents were obliged to disclose to complainant. A "material fact" is a fact that a reasonable person would be likely to attach significance to . . . in deciding whether to enter the commodity futures markets. *See Gordon v. Shearson Hayden Stone, Inc.*, COMM. FUT. L. REP. (CCH) ¶21,016 at 23,981-23,982 [1980-1982 Transfer Binder]. The duty of disclosure may vary with the nature of the broker-customer relationship. In this connection, the complainant did not rely entirely on Fromm's advice for trading decisions. For instance, he began trading the larger 5,000-ounce contracts instead of the 1,000-ounce contracts against Fromm's advice.

Although price limits generally may have some restraining effect on volatile price movements, they cannot be considered a major factor in such movements. And the specific rule in issue could hardly be expected to have any significant effect on market movements. The complainant was aware that price limits existed. Tr. 24. The subject rule allowed expanded limits after two consecutive limit moves. Thus, if the market closed down the 50 cents limit two days in a row, thereby reducing the value of a 5,000-ounce contract by $5,000, and then moved another 50 cents, lowering the contract value an additional $2,500, the rule permitted another 25-cent move equal to $2,500 per contract.

As noted, daily price limits do not prevent price movements. It is not credible that complainant, who was admittedly aware generally of the risks of trading commodity futures, and willing to assume those risks, would have been deterred from entering the market by knowledge of the contingency rule in question. Complainant has suffered severe losses, and has retrospectively attempted to establish a causal link between those losses and Fromm's unawareness of the expanded limit rule. His argument is not persuasive.

The complainant also claims that he was given false information about the expanded price limits, that in reference to the price movement in excess of 50 cents, Fromm informed him that he did not know what was "wrong". Fromm claims to have informed complainant of the expanded limits on the same day the question arose. This is confirmed by a letter complainant wrote on March 4, 1983, where he states "at 12:45 p.m. [on February 25, 1983] I was informed that New York expanded the down

limit to 75 cents and that a teletype was never sent of this change to [BEL] informing them of this very important fact." It is thus apparent that complainant was informed of the expansion of the trading limits on the day it occurred. The only possible question remaining on which doubt could have persisted was the precise authority for that action. Any inability to provide an explanation of this was not misrepresentation and it is not a matter that should have affected complainant's trading decisions.

Respondents' office order tickets show that a market order was entered for complainant on February 25, at 1:15 p.m. Complainant claims that the order was placed earlier when it may have been executed. According to him his wife called Fromm at about 12:30 p.m. and was informed that the market was down 52 cents. Thereafter, complainant avers that he called Fromm, and placed the order, "no later than 1:00 p.m." However, the price change register of COMEX shows that the contract in May '83 silver did not reach $13.10, 52 cents below the previous day's close, until approximately 1:44 p.m. (C.S.T.). Hence, the call of Mrs. Hlavinka would necessarily have occurred later than complainant asserts. Additionally, complainant stated in a document, submitted on March 1, 1984:

> We placed a sell order Friday, February 25, for both contracts. I and my wife, Mary Hlavinka, both spoke to John Fromm. I remember telling John Fromm he's (sic) got to get us out. He replied, I'll try, but it's locked in.

The COMEX price change register shows that the market did not lock down the limit on that day until about 1:07 p.m. (C.S.T.). This confirms that the order was

placed after complainant now claims that it was. His assertions are inconsistent, and his present position is contrary to the time stamp on the involved order. It is concluded, therefore, that he has not shown that respondents delayed placing this order. Since the market was locked down the limit when the order was placed, respondents are not responsible for its non-execution.

Under the involved trading rules, there is no limit on price movements in the current contract month. Contracts in further out months may be liquidated, though locked against a price limit, by executing a spread between such months and the current month. Despite the possibility of such a maneuver it can be costly to the customer. The complainant claims, and he is not disputed on this assertion, that he was not informed of this possible method of exiting from the market. It is far from clear, however, that complainant would have made this costly transaction if he had known it was possible. Market orders were placed, but not executed the next trading day, Monday, the 28th. On Tuesday he liquidated one contract, but did not enter a market order for the second contract until later on Tuesday, after a limit order failed to be executed. It is evident that complainant was not determined to close his positions at all costs, as he now maintains. Nor is it certain that his losses would have been less if he had spread out of his position. It is concluded that no calculable damages resulted from respondents' failure to recommend this course of action.

The complainant avers that he was informed that a quotation machine in BEL's office was out of order at this time, and that Fromm stated to him that the machine was too expensive to maintain. Respondents deny that any

such statement was made, and assert that if the machine had broken down it would have been serviced immediately. Even if complainant's version of this matter is accurate he has not shown any connection between this situation and his losses. He does not even allege that he was unable to obtain current market information from respondents at any time. It is concluded that complainant has not shown that he was damaged by any violation of the Act or Commission regulation of respondents.

ORDER

It is ordered that the complaint be, and is hereby DISMISSED.

Reported at CCH Commodity Futures L.R. §23,906 (1987)

UNITED STATES OF AMERICA
Before the
COMMODITY FUTURES TRADING COMMISSION

RONALD P. HLAVINKA, v. BLUNT, ELLIS & LOEWI, INC., HENRY JOHN FROMM, AND PETER J. PFEFFER	CFTC Docket No. 84-R117 ORDER OF SUMMARY AFFIRMANCE

Upon consideration of the briefs and the record as a whole, we are satisfied that the initial decision is substantially correct in result, and that no important question of law or policy has been raised on appeal. Accordingly, we have determined that the initial decision should be affirmed without opinion.[3] Respondents' motion to dismiss the appeal is denied.

In making this determination, we do not adopt the initial decision, including any rationale contained therein,

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[3] Complainant has not demonstrated any error in the judge's conclusion that the respondents' failure to inform him in advance of a change in the daily price limits of the Comex 5000 oz. silver futures contract was not an omission of a material fact. *See Sudol v. Shearson Loeb Rhoades, Inc.*, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶22,748 (CFTC 1985) (in circumstances presented, size of contract not a material fact). The record also supports the judge's conclusions concerning complainant's allegations of failure to disclose risk, failure to supervise, and failure to enter timely liquidation trades.

as our own. Neither the decision nor the fact of summary affirmance shall serve as Commission precedent in other proceedings. *See* 17 C.F.R. §12.406(b)(1984).

IT IS SO ORDERED.[4]

By the Commission (Acting Chairman HINEMAN and Commissioners WEST, SEALE, and DAVIS).

Lynn K. Gilbert
Deputy Secretary of the
Commission
Commodity Futures Trading
Commission

Dated: September 18, 1987

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[4] Under Sections 6(b) of the Commodity Exchange Act (7 U.S.C. Sections 9 and 18(e) (1982)), a party may appeal a reparation order of the Commission to the United States Court of Appeals for only the circuit in which a hearing was held; if no hearing was held, the appeal may be filed in any circuit in which the appellee is located. The statute also states that such an appeal must be filed within fifteen days after notice of the order.

Reported at 867 F.2d 1029

UNITED STATES COURT OF APPEALS
For the Seventh Circuit

No. 87-2652
RONALD P. HLAVINKA,

Petitioner,

v.

COMMODITY FUTURES TRADING COMMISSION,

Respondent.

On Petition for Review of An Order of The Commodity Futures Trading Commission

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ARGUED NOVEMBER 15, 1988 –
DECIDED FEBRUARY 6, 1989

Before CUMMINGS, WOOD, JR., and EASTERBROOK, *Circuit Judges.*

CUMMINGS, *Circuit Judge.* Petitioner Ronald P. Hlavinka seeks this Court's review of the Commodity Futures Trading Commission (CFTC) order affirming an Administrative Law Judge's denial of his reparations action against futures commission merchant Blunt, Ellis & Loewi, Inc. (Blunt Ellis) and its agents for losses he and his wife incurred in trading silver futures contracts. We deny Hlavinka's petition for review.

I.

Facts

In 1980, Hlavinka opened a non-discretionary commodity futures trading account with Blunt Ellis, a registered futures commission merchant in Milwaukee, Wisconsin. In doing so, Hlavinka signed a customer risk disclosure statement as required under the CFTC's Rules. See 17 C.F.R. §1.55. During the next year, he traded futures contracts and silver bullion. He discontinued trading in October 1981 but retained his account with Blunt Ellis. After the account executive who had been assigned to Hlavinka's account left Blunt Ellis in 1982, another of its employees, John Fromm, contacted Hlavinka to interest him in resuming his investments. As a result, he began trading again in August 1982.

In late 1982, Hlavinka expressed interest in trading 5000-ounce silver futures contracts. These contracts were traded on the Commodity Exchange (COMEX) in New York.[5] Fromm did not recommend this strategy but agreed to process Hlavinka's orders.[6] On January 10, 1983, Hlavinka purchased his first 5000-ounce COMEX silver futures contract. As of February 14, 1983, Hlavinka had profitably completed six additional trades.

On Friday, February 18, 1983, Hlavinka established a new position in the 5000-ounce contract market by

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[5] Until then, Hlavinka's investment in silver futures had been confined to the 1000-ounce contracts available on the Chicago Board of Trade.

[6] Blunt Ellis was not a member of COMEX. The firm hired ACLI International, Inc. (ACLI), a COMEX member, to fill its trading orders.

entering a "limit" order for one "long" May 1983 contract.[7] This order was filled at a price of $14.84 per ounce. The market was closed on the following Monday due to President's Day. Significantly, the market opened on Tuesday, February 22, at a lower price than the previous Friday's closing price. Under COMEX rules, the price of a given commodity can only fluctuate within a certain range in one trading day; for silver futures, the limit was then set at 50 cents.[8] By Tuesday's end, the market closed at the lower limit allowed under COMEX rules, or 50 cents down.

On Wednesday, February 23, the market opened in a "locked"[9] position, an indication that the market price of

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[7] A limit order is one "in which the customer sets a limit on either price or time of execution, or both, as contrasted with a market order which implies that the order should be filled at the most favorable price as soon as possible." A long contract is defined as: "(1) One who has bought a futures contract to establish a market position; (2) A market position which obligates the holder to take delivery; (3) One who owns an inventory of commodities." Glossary to S. Rep. No. 850, 95th Cong., 2d Sess. 3, reprinted in 1978 U.S. Code Cong. & Admin. News 2087, 2167. "[A] price increase would produce a gain for a 'long' speculator who had acquired a contract to purchase the same commodity with no intent to take delivery but merely for the purpose of reselling the futures contract at an enhanced price." *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353, 357-358.

[8] "The upper and lower limits . . . placed upon price movements in any given day for individual futures contracts serve to cool off hectic markets where prices might otherwise overreact to incomplete or inaccurate market information." 1 P. Johnson, *Commodities Regulation* §2.20, at 244 (1982).

[9] A "locked" position occurs when the market reaches the permitted up or down day's limit.

the silver was still declining. Hlavinka's wife (with his consent) entered a limit order to purchase one long May 1982 contract at $13.81 or better, and this order was filled.[10] Hlavinka and his wife now held two long May 1983 5000-ounce silver futures contracts. At the end of trading on February 23, the market had closed down 50 cents for the second consecutive day.

On February 24, 1983, Blunt Ellis received an opening call report from its COMEX agent, ACLI, listing the day's expected price movement limits for each COMEX contract. The ACLI report erroneously stated that the maximum price movement limit for a COMEX 5000-ounce silver futures contract would be 50 cents. In fact, the limit for the day was 75 cents.[11]

In a telephone conference on February 24, Hlavinka and Fromm decided to liquidate one of Hlavinkas' two long positions at a price of $13.91. Fromm placed the limit order seven minutes before the COMEX market closed. However, the order was not executed because the market price did not reach $13.91 during the remaining time. The order expired at the end of the market day and, as a result, the Hlavinkas retained both contracts.

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[10] Fromm marked this order as "unsolicited".

[11] This larger limit was due to a COMEX rule which provides that if the market closed at the maximum allowable limit for two consecutive trading days (as occurred on February 22 and 23), the price limit would expand to 150% of the normal limit. Should the trend continue and the market continue to expand, the rule specified that the limit would then extend to 200% of the original amount, or $1.00. This rule is designed to alleviate the locked market situation.

In its opening call report for Friday, February 25, 1983, ACLI again incorrectly reported to Blunt Ellis that the price movement limit for the day would be 50 cents. As the market opened, the market price for silver futures remained relatively stable. However, the price later dropped sharply at about the time Mary Hlavinka, petitioner's wife, called Fromm for a price report. When Fromm informed her that the price had dropped 52 cents from the opening quote, she questioned how this could have happened. Fromm was also troubled by the news, since he had understood that there was a 50-cent limit for the day. Fromm contacted ACLI and learned of the 75-cent expanded limit rule. When Fromm telephoned Mr. Hlavinka to explain the expanded price limit situation, he placed a market order to liquidate both his and Mary's contracts.[12] This order was not filled, however, since the market had already locked at the down limit price.

ACLI's opening call report for the next trading day (on Monday, February 28), correctly reflected a price movement limit of $1.00. At 8:45 in the morning (C.S.T.), Hlavinka placed a market order to sell both contracts, an order which remained unfilled since the market opened in a locked position and remained that way throughout the entire day. On Tuesday, March 1, Hlavinka placed a market order to liquidate the contract he acquired on February 18. Mrs. Hlavinka held onto the other contract in the belief that the market would be "corrected."

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[12] The order was time-stamped 1:15 p.m. (C.S.T.). The ALJ reported that the market locked down the limit at about 1:07 p.m. (C.S.T.).

Hlavinka's sell order was filled. Later on the same day, he directed Fromm to liquidate the second contract. By the time this order was placed, the market had already locked down. The second sell order was eventually filled the next day, March 2, at a price of $10.83.

The Hlavinkas lost $35,184.60 in trading the two contracts. He lost an additional $281.06 in trading a 1000-ounce silver contract on March 7, 1983. On December 2, 1983, he initiated a reparations action under Section 14 of the Commodity Exchange Act (CEA), codified at 7 U.S.C. §18, against Blunt, Ellis, Peter J. Pfeffer (Fromm's supervisor), and Fromm for damages. He asserted that the broker and its agents knew or should have known about the expanded limit rule, and that the failure to disclose this information caused him to suffer substantial losses. Specifically, Hlavinka claims that had he known of the rule, his wife would not have entered into the February 23 contract, and that he would have closed both positions on February 24. He also charged that the broker should have advised to spread his position to offset potential losses.[13]

The Administrative Law Judge (ALJ) who considered the case concluded that Blunt Ellis and its agents had not violated the anti-fraud provision of the CEA, see 7 U.S.C. §6b quoted in n.11 *infra*, and that information concerning the expanded price limit was not material. *Hlavinka v. Blunt, Ellis & Loewi, Inc.*, [1986-1987 Transfer Binder] COMM. FUT. L. REP. (CCH) ¶23,324 (Oct. 22, 1986). The

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[13] Hlavinka further argued that Fromm had delayed in executing some of his orders. He does not press this assertion on appeal.

ALJ observed that Hlavinka had been familiar with the market's price limits. In light of Hlavinka's awareness of market fluctuations and the risks of commodity trading, the ALJ was not persuaded by Hlavinka's assertion that he would have altered his investment strategy had he known of the expanded limit rule. Moreover, the ALJ pointed to a letter written by Hlavinka on March 4, 1983 in which the petitioner admitted that he had been told of the market's expanded limits on February 25, 1983. These factors caused the ALJ to rule against materiality.

The ALJ concluded that Hlavinka failed to establish causation between the omission and the market positions he and his wife had taken. The ALJ also ruled that no calculable damages resulted from the failure to advise Hlavinka to spread positions. Accordingly, the action was dismissed on October 22, 1986, and Hlavinka appealed to the CFTC. On September 18, 1987, the CFTC affirmed the ALJ's ruling without opinion. This appeal followed.

II.

Analysis

The exchange of commodity futures is governed by the CEA, codified at 7 U.S.C. §1 *et seq.*[14] Under the Act, an aggrieved customer can institute a reparations action against a futures commission merchant and its agents. 7 U.S.C. §18; *Commodity Futures Trading Commission v. Schor*, 478 U.S. 833, 836. Hlavinka's reparations action was

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[14] Commodities trading has been explained in *United States v. Dial*, 757 F.2d 163, 164-166 (7th Cir. 1985), certiorari denied, 474 U.S. 838. See also Fishman, *Commodities Futures: An Introduction for Lawyers*, 65 Chicago Bar Record 306 (1984).

brought under the anti-fraud provision, Section 4b of the CEA.[15] When reparations actions are reviewed by this Court, the CFTC's actual findings, "if supported by the weight of [the] evidence," are taken as conclusive. 7 U.S.C. §9; *Dohmen-Ramirez v. Commodity Futures Trading Commission*, 837 F.2d 847, 856 (9th Cir. 1988); *Drexel Burnham Lambert, Inc. v. Commodity Futures Trading Commission*, 850 F.2d 742, 746-747 (D.C. Cir. 1988). Indeed, the standard of review is very narrow.

> The function of this court is something other than that of mechanically reweighing the

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[15] Section 4b of the Act provides:

> It shall be unlawful (1) for any member of a contract market, or for any correspondent, agent, or employee of any member, in or in connection with any order to make, or the making of, any contract of sale of any commodity in interstate commerce, made, or to be made, on or subject to the rules of any contract market, for or on behalf of any other person . . .
>
> > (A) to cheat or defraud or attempt to cheat or defraud such other person;
> > (B) willfully to make or cause to be made to such other person any false report or statement thereof, or willfully to enter or cause to be entered for such person any false record thereof;
> > (C) willfully to deceive or attempt to deceive such other person by any means whatsoever in regard to any such order or contract or the disposition or execution of any such order or contract, or in regard to any act of agency performed with respect to such order or contract for such person . . . .
>
> 7 U.S.C.§6b.

> evidence to ascertain in which direction it "preponderates"; it is rather to review the record for the purpose of determining whether the finder of fact – here the ALJ – was justified.

Chapman v. United States Commodity Futures Trading Commission, 788 F.2d 408, 410 (7th Cir. 1986)(per curiam) (citations omitted).

Hlavinka does not argue that the broker willfully withheld information. Rather, he claims that Fromm breached his fiduciary duty and acted negligently.[16] Hlavinka points to the fact that he always carried a "beeper" with him as proof of his intent and ability to make instantaneous market decisions. Since Blunt Ellis is not a discount brokerage firm, Hlavinka maintains that the firm had a duty to advise him fully of the market's changes and its attendant risks, and that he relied on respondents to do so. Hlavinka also complains that Fromm should have directed him to spread his and his wife's positions in order to minimize losses. Accordingly, he contends that the ALJ should not have dismissed his claims.

In this case, the ALJ found no breach of fiduciary duty. Whether an advisor's role is that of a fiduciary depends on:

> whether the customer is relying on [the commodity professional's] expertise and judgment in either entering the market or in making trading decisions. Where the professional's role is not of that nature, such as where the customer

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[16] If true, the other respondents would be liable to Hlavinka under the theory of *respondeat superior*. Section 2a(1) of the CEA, 7 U.S.C. § 4; *Bosco v. Serhant*, 836 F.2d 271, 280 (7th Cir. 1987).

> makes his own independent trading decisions and the professional's role is therefore largely clerical, the duty to disclose material facts is less. . . .

2 P. Johnson, *Commodities Regulation* § 5.49, at 353-354. (1982). The ALJ noted that Hlavinka did not rely entirely on Fromm's advice in conducting his trading. In fact, the decision to speculate in the 5000-ounce silver market was Hlavinka's alone, and there was evidence that at least one of the executed orders was "unsolicited" by Fromm. The ALJ also determined that Hlavinka knew of the risks involved in trading silver futures, and that he had learned of the expanded price limit rule on February 25. In these circumstances there is no need to disturb the ALJ's finding that Hlavinka failed to establish a breach of fiduciary duty.

There is also no basis for Hlavinka's claim of negligence. As we have recently held, "for commodities fraud, negligence is not enough." *Tamari v. Bache & Company (Lebanon) S.A.L.*, 838 F.2d 904, 908 (7th Cir. 1988). To the same effect see also *Hill v. Bache Halsey Stuart Shields Inc.*, 780 F.2d 817, 822 (10th Cir. 1986). Of course, Hlavinka could prevail by showing that the broker was reckless and that the withheld information was material. *Drexel Burnham Lambert, Inc.*, 850 F.2d at 748; *First Commodity Corporation of Boston v. Commodity Futures Trading Commission*, 676 F.2d 1 (1st Cir. 1982); see also *Flaxman v. Commodity Futures Trading Commission*, 697 F.2d 782, 787 (7th Cir. 1983) (standard of "willfulness" includes careless disregard).[17] However, this possibility was foreclosed

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[17] Although tension exists between the "careless disregard" language of *Flaxman* and that of more recent cases, e.g.,

(Continued on following page)

because, as the ALJ properly ruled, the expanded limit rule was not material information in the present case.

The critical inquiry for materiality is what effect the failure to apprise Hlavinka of the expanded limit rule might have had on his decision to stay in the market. See *TSC Industries, Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (materiality is determined by whether there was a "substantial likelihood that, under all the circumstances, the omitted fact would have assumed actual significance in the deliberations of the reasonable [investor]").[18] The ALJ's conclusion that Hlavinka's losses were not caused by the broker's failure to tell him of the expanded limit rule was appropriate. The ALJ correctly observed that while price limits have a restraining effect on volatile price movements, they do not cause the movements. The Hlavinkas' losses were due to the declining price of silver futures, not to the rule's application. "[I]t may be impossible for [the customer] to liquidate his position on market days when trading is inactive due to the fact that the price has risen or fallen to the exchange's daily maximum allowed change for that day." 1 P. Johnson, *supra*, § 3.107,

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(Continued from previous page)

McLaughlin v. Richland Shoe Company, 108 S.Ct. 1677, there is no need to address this issue here.

[18] Unfortunately, "[t]ests of materiality of misrepresentations, omissions, false reports, etc. have not yet evolved in commodities law. When they do, they should approximate the important-to-a-reasonable investor (or trader) test of 10b-5 and the securities laws." 1 A. Bromberg & L. Lowenfels, *Securities Fraud & Commodities Fraud*, § 4.6, at 82.370 (1988); see also *Saxe v. E.F. Hutton & Company, Inc.*, 789 F.2d 105, 111 (2d Cir. 1986). Therefore, reliance on *Northway* is appropriate.

at 552. While application of the expanded limit rule allows a market greater range in which to operate, when the market is declining (as occurred here), the price will soon lock down. As one commentator noted,

> [D]aily price fluctuation limits do not necessarily affect the market *trend*, . . . and it frequently happens that, when a major market development occurs, a futures contract will experience successive "limit up" or "limit down" days until the price adjusts fully to that news. A serious side effect of successive limit up or limit down days is that persons suffering losses may be unable to liquidate their positions as trading promptly reaches the maximum price limit and, with market participants unwilling to accept a price within the permissible range, trading ceases until the next day when the new limit is in force. This experience can be repeated for a number of trading sessions and losses can be greatly amplified.

1 P. Johnson, *supra*, § 220, at 244-245 (emphasis in original). Furthermore, although Hlavinka attempted to liquidate once he learned of the expanded limit situation, he later decided to return one of the contracts. Thus it is clear that Hlavinka's market strategy was not influenced by his knowledge of the expanded limit rule.

Finally, the ALJ was correct in finding that no fraud occurred in the failure to direct Hlavinka to spread his investment. In fact, such a strategy is not always effective in reducing an investor's loss, as indicated in the risk disclosure statement given to Hlavinka by Blunt Ellis. See also *Hill*, 790 F.2d at 824 (noting that courts are reluctant

to find fraud where customers have received risk disclosure documents). For these reasons, Hlavinka's petition for review is denied.

A true Copy:

Teste:

Clerk of the United States Court of Appeals for the Seventh Circuit

STATUTES

7 U.S.C. § 18 (1983)

§ 18. Complaints against registered persons

(a) Petition for actual damages

Any person complaining of any violation of any provision of this chapter, or any rule, regulation, or order issued pursuant to this chapter, by any person who is registered under this chapter may, at any time within two years after the cause of action accrues, apply to the Commission for an order awarding actual damages proximately caused by such violation.

(b) Rules and regulations; control over right of appeal

The Commission may promulgate such rules, regulations, and orders as it deems necessary or appropriate for the efficient and expeditious administration of this section. Notwithstanding any other provision of law, such rules, regulations, and orders may prescribe, or otherwise condition, without limitation, the form, filing, and service of pleadings or orders, the nature and scope of discovery, counterclaims, motion practice (including the grounds for dismissal of any claim or counterclaim), hearings (including the waiver thereof, which may relate to the amount in controversy), rights of appeal, if any, and all other matters governing proceedings before the Commission under this section.

* * *

(e) Review

Any order of the Commission entered hereunder shall be reviewable on petition of any party aggrieved thereby, by the United States Court of Appeals for any circuit in which a hearing was held, or if no hearing was held, any circuit in which the appellee is located, under the procedure provided in Section 9 of this title. Such appeal shall not be effective unless within 30 days from and after the date of the reparation order the appellant also files with the clerk of the court a bond in double the amount of the reparation awarded against the appellant conditioned upon the payment of the judgment entered by the court, plus interest and costs, including a reasonable attorney's fee for the appellee, if the appellee shall prevail. Such bond shall be in the form of cash, negotiable securities having a market value at least equivalent to the amount of bond prescribed, or the undertaking of a surety company on the approved list of sureties issued by the Treasury Department of the United States. The appellee shall not be liable for costs in said court. If the appellee prevails, he shall be allowed a reasonable attorney's fee to be taxed and collected as a part of his costs.

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7 U.S.C. § 25 (1983)

§ 25. Private rights of action

(a) Actual damages; actionable transactions; exclusive remedy

(1) Any person (other than a contract market, clearing organization of a contract market, licensed board of

trade, or registered futures association) who violates this chapter or who willfully aids, abets, counsels, induces, or procures the commission of a violation of this chapter shall be liable for actual damages resulting from one or more of the transactions referred to in clauses (A) through (D) of this paragraph and caused by such violation to any other person –

(A) who received trading advice from such person for a fee;

(B) who made through such person any contract of sale of any commodity for future delivery (or option on such contract or any commodity); or who deposited with or paid to such person money, securities, or property (or incurred debt in lieu thereof) in connection with any order to make such contract;

(C) who purchased from or sold to such person or placed through such person an order for the purchase or sale of) –

(i) an option subject to section 6c of this title (other than an option purchased or sold on a contract market or other board of trade);

(ii) a contract subject to section 23 of this title; or

(iii) an interest or participation in a commodity pool; or

(D) who purchased or sold a contract referred to in clause (B) hereof if the violation constitutes a manipulation of the price of any such contract or the price of the commodity underlying such contract.

(2) Except as provided in subsection (b) of this section, the rights of action authorized by this subsection and by

sections 7a(11), 18, and 21(b)(10) of this title shall be the exclusive remedies under this chapter available to any person who sustains loss as a result of any alleged violation of this chapter. Nothing in this subsection shall limit or abridge the rights of the parties to agree in advance of a dispute upon any forum for resolving claims under this section, including arbitration.

* * *

(c) Jurisdiction

The United States district courts shall have exclusive jurisdiction of actions brought under this section. Any such action must be brought within two years after the date the cause of action accrued.

ANTI-INJUNCTION ACT

28 U.S.C. § 2283

§ 2283. Stay of State court proceedings

A court of the United States may not grant an injunction to stay proceedings in a State court except as expressly authorized by Act of Congress, or where necessary in aid of its jurisdiction, or to protect or effectuate its judgments.

COMMODITY FUTURES TRADING COMMISSION REGULATIONS

17 C.F.R. § 12.13 (1984)

12.13 Complaint; election of procedure.

(a) *In general.* Any person complaining of a violation of any provision of the Act or a rule, regulation or order of the Commission thereunder by any person who is a registrant (as defined in § 12.2(y)) may, at any time within two years after the cause of action accrues, apply to the Commission for a reparation award by filing a written complaint which satisfies the requirements of this rule.

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17 C.F.R. § 12.15 (1984)

§ 12.15 Notification of complaint.

(a) *Forwarding of complaint to registrant.* If, in the opinion of the Director of the Office of Proceedings, the facts set forth in a complaint warrant such action as to any of the registrants, a copy of complaint, together with any attachments thereto, shall be forwarded by serving by registered mail or certified mail any such registrant named therein at an address previously designated with the Commission by the registrant for receipt of reparation complaints, as provided in Commission Regulation 17 CFR 3.30, or, if no such designation has been filed with the Commission, at such address as will accomplish actual notice to the respondent. Should the Director determine to forward the complaint, the complainant shall be

notified of this determination at the time the complaint is forwarded.

(b) *Determination not to forward complaint.* The Director may, in his discretion, refuse to forward a complaint as to a particular respondent if it appears that the matters alleged therein are not cognizable in reparations, or that grounds exist pursuant to § 12.24(c) or (d) for refusing to forward the complaint. If the Director of the Office of Proceedings should determine not to forward the complaint to all registrants named in the complaint in accordance with this Section, no proceeding shall be held thereon and the complainant shall be notified to that effect.

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17 C.F.R. § 12.24 (1984)

§ 12.24 Parallel proceedings.

(a) *Definition.* For purposes of this section, a parallel proceeding shall include:

(1) An arbitration proceeding or civil court proceeding, involving one or more of the respondents as a party, which is pending at the time the reparation complaint is filed and involves claims or counterclaims that are based on the same set of facts which serve as a basis for all of the claims in the reparations complaint, and which either:

(i) Was commenced at the instance of the complainant in reparations; or

(ii) Involves counterclaims by the complainant in reparations alleging violations of the Commodity Exchange Act, or any regulation or order issued thereunder; or

(iii) Is governed by a compulsory counterclaim rule of federal court procedure which required the complainant in reparations to assert all of his claims (including those based on alleged violations of the Commodity Exchange Act, and any regulation or order issued thereunder) as counterclaims in that proceeding;

* * *

(c) *Effect of pending arbitration or civil court litigation.* (1) The Director of the Office of Proceedings shall refuse to institute an elected decisional procedure concerning a reparation complaint filed under this part in which there is a parallel proceeding described in paragraph (a)(1) of this section and shall return the complaint to the complaining person. The effective date of the Director's termination of the complaint without prejudice shall be fifteen (15) days from the date of service of notice of the action taken pursuant to this paragraph.

(2) If notice of a parallel proceeding described in paragraph (a)(1) of this section is received before the initial decision is filed (or before a final decision under § 12.106 of the rules is entered), a proceeding in which a decisional procedure has been commenced shall be dismissed, without prejudice. The effective date of the order of dismissal shall be fifteen (15) days from the date of service of the order by the Proceedings Clerk.

(e) *Exceptions.* At the time notice of a parallel proceeding is filed pursuant to paragraph (b) of this section, or

any time thereafter, any party, or the receiver or trustee, may file and serve upon other parties a statement in support of or in opposition to any action taken or to be taken pursuant to paragraph (c) or (d) of this section. This statement shall be addressed to the Office of Proceedings, attention of the Proceedings Clerk. Upon receipt of any such statement, the Proceedings Clerk shall immediately forward the statement to the official with responsibility over the case. The notice and the statements filed by the parties shall be reviewed by that official who, on or before the effective date of action taken pursuant to paragraphs (c)(1), (c)(2), (d)(1), and (d)(2), of this section, may take such actions as, in his opinion, are necessary to ensure that the parties to the matter or proceedings are not unduly prejudiced.